November 29, 2017 – Pressure Building

I made passing reference on Monday to a topic Iâ??d like to discuss further today, namely, my sense that pressure is building in the pricing mechanism and structure of the silver and gold markets. First, what do mean by pressure is building? I see signs, some of which Iâ??ll comment on today, which indicate growing stress underlying what has been a recent period of price movement that has been quite stable. Moreover, silver and gold price stability has come in the face of most other markets, as stocks and crypto currencies moved higher.

It should come as no surprise that my main indicator of pressure lies in the current positioning of the managed money traders against the commercials in COMEX silver and gold futures contracts. As I have been intoning for months, there must be some type of resolution to what has to be considered an extreme market structure in both gold and silver. The passage of time alone does nothing to resolve an extreme market structure; only the actual buying or selling of COMEX futures contracts. To cut to the chase, the specific extreme positioning revolves around the managed money net long position and the commercial net short position, particularly the concentrated short position of the 8 largest commercials.

While it is certainly possible that the net positioning on either side could grow larger on new price highs ahead, that will only postpone an inevitable more fully complete resolution. What has to happen eventually is that the commercials will succeed in inducing the managed money traders to sell out a substantial portion of their current long positions and also to add new shorts on lower prices or that the commercials will not succeed or not fully succeed.

Since the commercials have always succeeded in the past in rigging prices low enough to trip off eventual managed money long liquidation and new shorting, that has to be considered the high probability bet. And based upon the price action this morning, it would appear the commercials have been trying to do just that. But even though the commercialsâ?? trading record is near perfect, someday the pattern is bound to break and it will be the big shorts on the losing end. At least thatâ??s all part of this pressure thing. Let me run through some signs of why I think a break in pattern may be upon us.

Over the past three years or so, a distinct pattern has developed in both COMEX gold and silver futures that is quite pronounced â?? the magnitude of managed money positioning has reached extreme and I would say absurd levels. In other words, what I claim is the primary price driver, COMEX positioning, has grown much stronger than ever before. I report on this on a continual basis, so sometimes one needs to step back to get a better perspective.

Since 2014, there have been about a dozen documentable instances of net buying or selling by the managed money traders in COMEX silver where as many as 50,000 to 100,000 net contracts have been either bought or sold in fairly short periods of time. In COMEX gold futures, there have been about a dozen instances of the managed money traders buying or selling as many as 100,000 to nearly 200,000 net contracts. These are enormous quantities in real world equivalents; anywhere from 250 million to 500 million oz in silver and 10 million to 20 million oz in gold.

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COMEX silver or gold, the price of each rose, usually on the order of a few dollars in silver and $100 to $200 in gold. Each and every time the managed money traders sold such quantities, the price of either metal fell by those same rough dollar amounts. There has never been a time when the managed money traders have bought or sold such quantities where the price didnâ??t move up or down accordingly. In essence, this is the case upon which the claim that paper contract positioning is driving and setting prices is based.

Of course, the managed money traders canâ??t buy and sell in a vacuum and the enormous quantities that they transact are always taken by the commercials (or nearly so, as other traders have also started to take the other side of the managed money traders). Not only do the commercials take the other side of whatever the managed money traders buy or sell, there are numerous indications that the commercials are prodding and baiting the managed money traders into buying or selling (since the commercials basically control short term pricing). Since the commercials have clearly been the beneficiaries of the managed money positioning (with the 8 largest shorts always profitable), it is most reasonable to assume that the commercials are in control. Nothing new here.

What does appear to be new is that while the changes in managed money positioning have never been larger and while prices have always moved higher when these traders buy and have moved lower when they sold, the extent of the price changes has diminished. In other words, the magnitude of managed money positioning has increased but price change has not. Let me use silver as an example, since everything is most always more extreme in silver.

This year we established both new record (as in all-time) managed money long positions in COMEX silver in April, as prices rose to $18.50 on that buying; as well as new record managed money short positions three months later in July as prices fell below $15.50. On the three dollar price decline from April to July, more than 100,000 net managed money silver contracts were sold. Iâ??m sure I commented at the time that the sale of 500 million oz of silver equivalent in less than 3 months was solely responsible for the price drop. The only wonder was why prices didnâ??t fall even more than $3 and the only answer for that is that the commercials were very aggressive in buying every contract the managed money traders sold.

On the subsequent $2.50 silver price rally into Sept, the managed money traders bought more than 83,000 net contracts or more than 415 million equivalent oz of silver. Look, itâ??s not possible that the purchase or sale of what is the equivalent of 50% of annual world mine production in a couple of months isnâ??t going to greatly impact the price of any world commodity. Of course, there are no instances, away from COMEX silver, where such large quantities have ever been bought or sold in any commodity. Again, the wonder is how could the buying of more than 400 million oz of silver within two months only result in a $2.50 (16%) price rise? The answer, once again, is the aggression of the commercials in selling to the managed money traders on that rally.

Whatâ??s new is that larger managed money positioning is having less relative price influence in terms of the magnitude of the price move. To be clear, this positioning is still the sole price driver, but larger quantities are not translating into larger moves. I see this as pressure building and as a pattern that must eventually be broken. At this point, the positioning has passed the absurd stage. 50% of annual world production being bought and sold within months is absurd on its face and such quantities only resulting in price changes of 2 or 3 dollars is even more absurd. Whatâ??s next â?? half a billion ounces of silver being bought or sold on a dollar price move? I donâ??t think thatâ??s in the cards, or alternatively, should it occur it will signify we are at or close to the end of this paper manipulation.

After the managed money traders bought the 83,000 net contracts causing silver prices to rise to just over $18 in early Sept, they have only sold around 15,000 contracts on the $1+ price decline through the last COT report. More importantly, since silver has spent much more time trading below its key 50 and 200 day moving averages than above, the new wonder is why havenâ??t the managed money traders sold much more by now?Â As you know, this is the question Iâ??ve been asking myself continuously. Maybe todayâ??s attempt to crack prices lower may finally result in aggressive managed money selling, but up until now that hasnâ??t been the case.

Already we have broken recent patterns in that the record positioning changes seen in silver this year occurred in short time frames, two or three months. The past two months has seen no big positioning change in silver, despite the downward penetration of key moving averages. Have the managed money traders finally awoken to the realization that they have been the mark at the poker table? I wish I knew, but I donâ??t. And as I just indicated, maybe weâ??re starting the long anticipated flush of the managed money traders to the downside. Time will tell. My point is if the managed money traders donâ??t sell aggressively, particularly in adding new shorts, then I canâ??t see how the 8 big commercial shorts can reduce their concentrated short position. If the managed money traders donâ??t sell, the 8 big silver shorts canâ??t buy (without causing prices to explode). This type of pressure hasnâ??t existed before, or certainly not to this extent.

Other recent happenings seem to add to the pressure is building premise. A report from Reuters assesses the sale of the ScotiaMocatta precious metals unit by Scotiabank. One thing that caught my eye was that the reason for the sale was changed from the previously reported cover story of some type of gold smuggling scandal to the much more reasonable version of poor financial returns and questions of legal liability from various gold and silver lawsuits alleging manipulation.

https://www.reuters.com/article/us-bank-nova-divestiture-goldman-sachs/goldman-sachs-among-bidders-for-scotiabanks-metals-unit-sources-idUSKBN1DS2C5

Of course, there was no mention of the potential liability that might accrue to Scotia or anyone which bought the unit as a result of being heavily short COMEX silver (and gold), but there was no chance that would be acknowledged by the bank. After all, the point is to put as much lipstick on this pig as possible and not scare away potential buyers. Still, I get the impression that Scotia is not waiting for a sale to rid themselves of the liability of being a big short caught on the wrong side of a big silver move higher.

As I mentioned on Monday, JPMorgan has taken a disproportionately larger share of the concentered short position of the 4 and 8 largest shorts in COMEX silver. My sense is that JPMorgan increased its paper short position out of necessity, as opposed to choice. Should ScotiaMocatta or any of the other large shorts in silver decide to reduce their short position, unless the prime manipulator, JPM, takes up the slack, silver prices will rise. JPMorgan is certainly positioned for an upside explosion in the silver price by virtue of its massive physical long position, but obviously felt compelled to cap silver prices at this time. More pressure.

Finally, the new report on securities short positions indicated a big jump in the short positions of SLV, the big silver ETF, as well as in GLD, the big gold ETF. As of Nov 15, the short position in SLV increased by 4.5 million shares to 20.1 million shares (ounces). The short position in GLD rose by 2 million shares to 12.6 million shares (1.2 million oz).

http://shortsqueeze.com/?symbol=SLV&submit=Short+Quote%E2%84%A2

This is the highest level of short positions in these securities in quite some time and negative on its face. In terms of COMEX-equivalent amounts, the increase in SLV comes to 900 COMEX contracts and the total short position is equal to 4000 COMEX contracts, just to keep things in perspective. In GLD, the increase in shorting was equal to 2000 COMEX gold contracts and the total short position is equal to 12,000 COMEX contracts.

As a percent of total shares outstanding, the short position in SLV is equal to 6%, a very large amount, while the equivalent percentage in GLD is in the 4.4% range, also large. To my mind, there should be no short position in these securities, because that means that 6% of SLV shares of have no metal backing, as required by the terms of the prospectus. I havenâ??t changed my mind about the short position in SLV, but I donâ??t wish to rehash the issue today. I am convinced that others, led by BlackRock, the worldâ??s largest asset manager, with over $5 trillion (with a â??tâ?•) in total assets and the sponsor of SLV, would not allow a total short position in the trust of just over $300 million to go â??badâ?•. The market capitalization of BlackRock stock itself is $80 billion and thereâ??s no way it would not stand behind SLV because that would jeopardize its ongoing business. All in my opinion, of course.

The bigger issue is that the short position in SLV (and GLD) is in synch with the extremely large commercial short position on the COMEX, as is typically the case. In other words, large short positions in SLV usually coincide with large commercial net short positions on the COMEX. While the short position in SLV is much smaller than the COMEX short position and, therefore, less impactful on price, the short SLV position is more â??physicalâ?• in nature than COMEX shorts. By this I mean that physical silver is â??owedâ?• to the trust when shares are shorted, where the case in COMEX short sales is that little real silver is owed since the vast majority of paper longs arenâ??t interested in taking physical delivery of metal.

On the other hand, short sales of SLV (and GLD) imply that physical metal may be unavailable or hard to obtain (at the right price) and this adds a new dimension in terms of pressure. If we ever do get what Izzy Friedman called the â??full pants downâ?• or a commercial failure in terms of an inability to cover short positions on lower prices, then a concurrent large short position in SLV can only add to the pressure on the shorts.

As far as what Fridayâ??s new Commitments of Traders (COT) Report might indicate, once again, Iâ??m going to refrain from any predictions because the data I look at are so mixed. There have been very sharp declines in total open interest, particularly yesterday in gold, but that liquidation looks to be of the spread variety into tomorrowâ??s first notice of delivery day on the big December contracts in gold and silver. Price action alone would suggest some further increase in commercial shorting in gold and the opposite in silver (based upon yesterdayâ??s price decline in silver). Gold remained above both of its key moving averages during the reporting week, while silver finished below its key moving averages in yesterdayâ??s trade. Still, this weekâ??s report is one to be analyzed, rather than handicapped.

Of more significance is todayâ??s price action in which silver set (slight) new lows for the past three months and is once again decisively below both key moving averages. This intensifies the question of whether the managed money traders can be induced into selling much more aggressively than they have to date. While gold is down today, it is still way above its 200 day moving average. The pressure is building for some type of resolution of the market structure and Iâ??m still of the opinion that a very large up move is going to unfold, either with one final flush out to the downside or not.

Ted Butler

November 29, 2017

Silver – $16.55Â Â Â Â Â Â (200 day ma – $17.15, 50 day ma – $17.00)

Gold – $1285Â Â Â Â Â Â Â Â (200 day ma – $1267, 50 day ma – $1286)

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